



Lynx Capital Group Ltd

Disciplined Strategic Investment Management

<http://www.lynxcap.com>

Market outlook as of October 2024

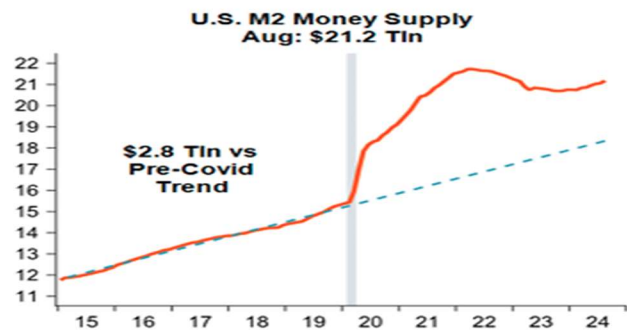
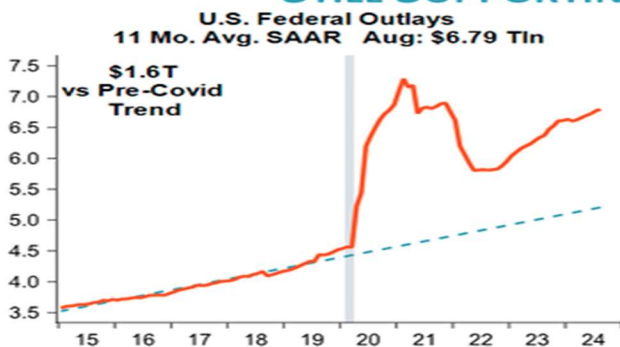
*“A fanatic is one who can’t change his mind and won’t change the subject”
Sir Winston Churchill (1874 – 1965), A British Statesman and war time Prime Minister.*

Overview

This year all sectors are up for the year, with the magnificent 7 technology firms contributing significantly to returns, which was largely driven by AI potential. We remain constructive on the profit prospects for the U.S. as lower rates should promote more broad-based growth. **Double-digit earnings growth for the S&P 500 in 2025** is priced in by the markets. The S&P 500 P/E is currently 26.2, which is historically high but below the 30ish level that was dominant in 2021 and in 1999-2000. The S&P 500 index trades at a premium valuation due to its increased technology exposure and highly adaptive companies the world has not seen the likes of in the past.

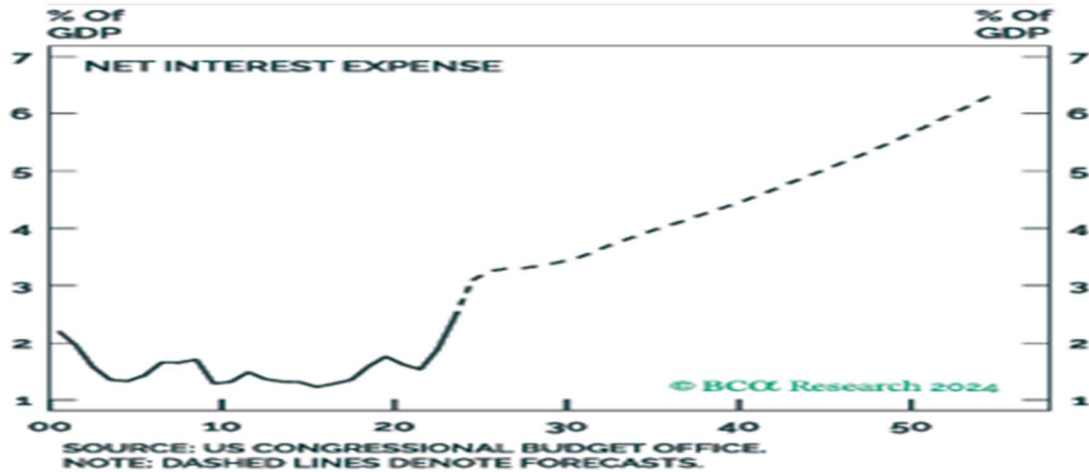
The economy has shown itself to be more resilient than anticipated, due primarily to two factors. The enthusiasm around AI and residual stimulus provided by various government programs such as Covid relief and the CHIPS and Infrastructure acts. Continued earnings growth, robust corporate capital expenditures, and unused government stimulus should keep the economy headed for a soft landing. Research shows that on average, **artificial intelligence** may boost productivity by 14% over the next decade.

LEVELS MATTER: EXCESSIVE FEDERAL OUTLAYS & M2 STILL SUPPORTING NOMINAL GROWTH.



Election uncertainty, budget deficits and issues going forward: Investors are paying close attention to **the impending election** as well as future Fed policy for the possibility of a soft landing. Sensational media coverage only serves to heighten market volatility. However, it's critical to look past the election and maintain awareness of issues confronting both investors and the incoming administration who ever that may be. The next administration will have to deal with multiple global geopolitical issues in the Middle East and Ukraine, while avoiding world war three.

With bond yields exceeding 4%, **the budget deficit standing at 7% of GDP**, and the federal **government debt on an unsustainable path**, a significant number of moderate, fiscally conservative Republicans will be against any measures that would worsen the fiscal picture. Today's high debt levels will be deflationary **because spending cuts will be needed** to cover increasing interest payments if the Fed does not inflate away the debt.

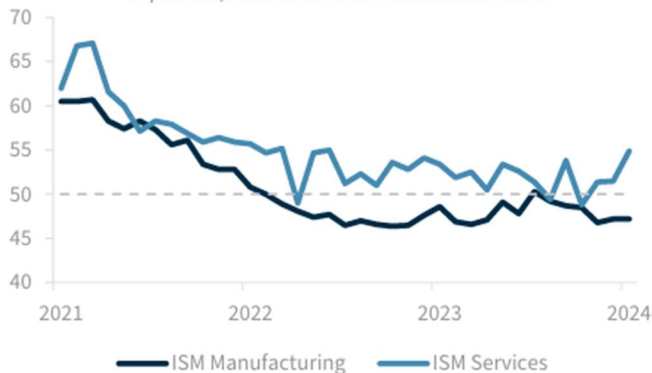


Regardless of the election outcome, the national debt, tariffs, and the expiration of the 2017 Tax Cuts and Jobs act in 2025 are important policy considerations that are on everyone’s radar. Both candidates are campaigning for policies that would increase the deficits. It would be good for both parties to remember and heed the lesson learned from the British Prime Minister Liz Truss and what is now called a ”Truss Moment” (*This is exactly what transpired in the UK in late September 2022 following the introduction of a budget by former Prime Minister Liz Truss that was primarily focused on tax cuts, deregulation and borrowing so alarmed global investors that the value of the British pound sank to a record low against the U.S. dollar. The Bank of England stepped in to prop up government bonds, an extraordinary intervention to calm the markets. The response left no doubt that her free-market ambitions were untenable. In a humiliating reversal, she was forced to reverse virtually all the tax cuts that week, including a much criticized one on high earners. She resigned after only 45 days in office*)

We are witnessing a world of “**haves and have-nots**” in this economic cycle. Washington policy was sufficiently restrictive stifling smaller enterprises and low-end consumers, but the surplus liquidity that resulted from it, spilled into the wallets of high-end consumers through rising asset prices and investment income. This kind of division is still occurring. Examine how the Manufacturing and Service industries have diverged – see charts below courtesy RJF and Bloomberg respectively.

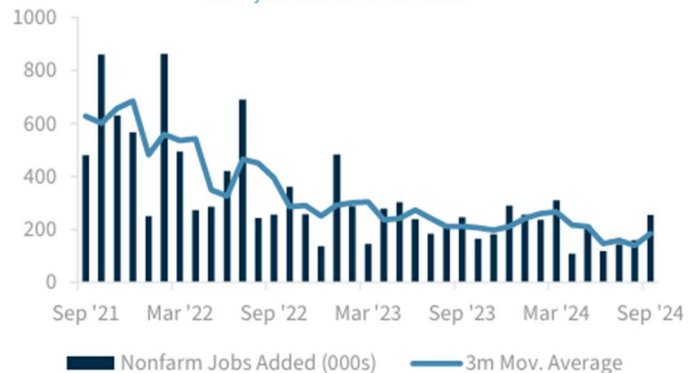
PMIs Diverge Further In September

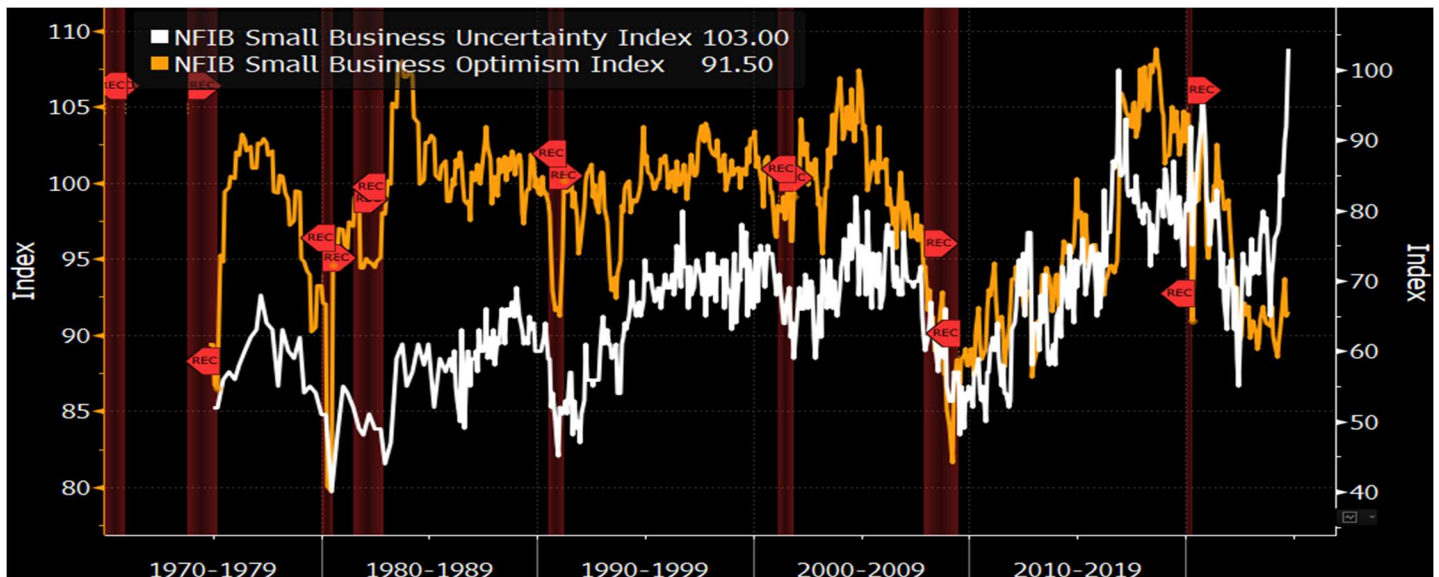
The ISM Manufacturing PMI remained unchanged at 47.2 in September, while ISM Services PMI increased to 54.9.



A Strong Employment Report

Nonfarm employment surged by 254,000 in September—the highest rate of job additions since March.





As the fed is primarily targeting wage inflation, we think this will be easier said than done as there is still a shortage of labor. Recently the *Longshoreman union demanded and got a 62% salary increase over six years, or 10% annually!* Additionally, talks to halt automation and maintain zero productivity growth are ongoing. Although union employment only makes up around 10% of the workforce there are numerous large union compensation packages with large increases in wage agreements which will inevitably have a spillover effect on prices. Recently a UPS drivers deal was reached in July, resulting in full-time workers' compensation reaching \$170,000 annually. Boeing workers are also now on strike, even with the company on its knees from previous missteps.

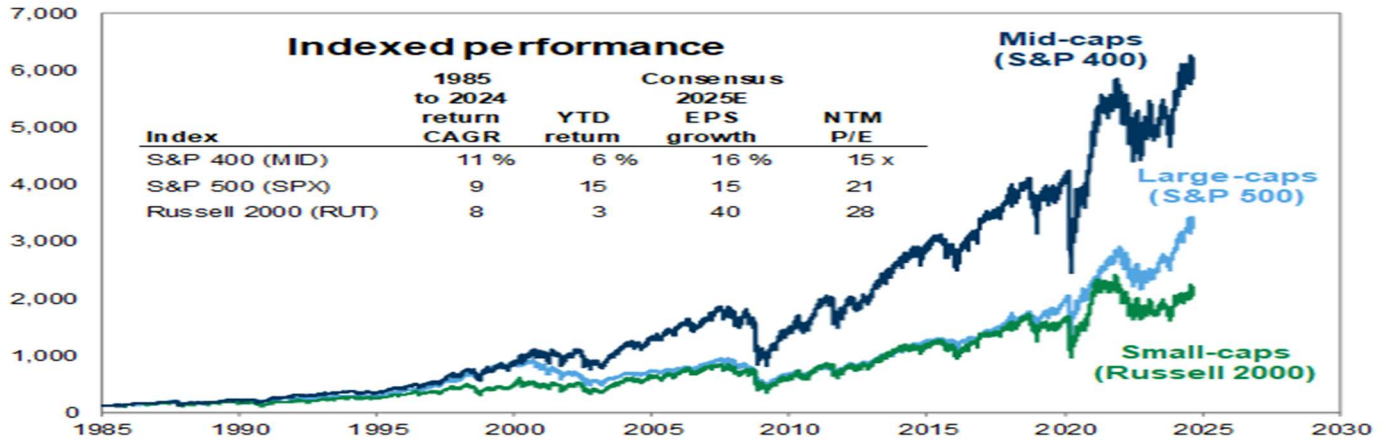
Delving further: Projections show that in the 2030s, *China's* economy is expected to overtake that of the United States as the largest in the world. We see rising protectionism between these heavyweights, with a focus on rivalry in the innovative and technological fields, including semiconductor chips and artificial intelligence. China will need budgetary assistance in order to meet its economic objectives. Due to its export-oriented economy, the Eurozone stands to gain greatly if the latest reforms are successful. China's economic rebound will likely increase demand for commodities, raising prices globally and putting more pressure on inflation. **Both superpowers are in a contest vying for key access to Strategic Resources:** In our increasingly digital environment, there is a focus on the need for critical resources such as rare earth metals and lithium for electric vehicles. Through 2030, there will likely be a 2.4% yearly growth in the demand for power. Higher energy prices that probably will occur in December due to low energy prices at Q4 of 2023 could exacerbate inflation.

Market outlook - We like the opportunity that *Mid-cap Stocks present* - Large-cap technology equities have seen some of the sharpest growth in earnings so far this year. *Mid-cap* stocks have outperformed large-cap stocks since August, when investors started to anticipate monetary easing. Given mid caps' substantial discounted valuation in comparison to large caps, relative performance should continue to improve.

Mid-cap value stocks are the sweet spot in terms of getting the best of both worlds. These companies are more mature than a lot of small-cap firms and have more attractive and stable profitability and cash flows. Mid-cap stocks have typically outperformed both large-caps and small-caps during the 12 months following the first Fed rate cut in an easing cycle. The S&P 400 also has a more balanced sector composition than the S&P 500, with greater exposure to industrial and financial stocks — two groups that are closely tied to the health of the economy.

Today, mid-cap equities offer investors superior earnings growth at a reasonable price compared with large caps. S&P 400 earnings growth has historically outpaced S&P 500 EPS growth and analyst consensus expects this growth superiority to continue in 2025 and 2026. Consensus expects mid-cap earnings to grow at an 11% compounded annual growth rate (CAGR) over the next two years compared with a 7% CAGR for the S&P 500.

Long-term performance of mid-caps, large-caps, and small-caps as of September 9, 2024



Source: Goldman Sachs Global Investment Research

For more risk averse investors, “There Are Reasonable Alternatives” (TARA) including short term treasuries and high-quality government and corporate bonds due to higher interest rates. – Please call us if you feel that you want to take less risk going forward or discuss your current asset allocation.

It is always advisable to review one’s individual circumstances and tolerance for risk. If any of your financial circumstances have changed, or you want to adjust your portfolios risk profile we always encourage you to contact us should you want to make any changes to your portfolio allocation.

As always, please feel free to contact us with any questions or concerns.

Brian

Brian Chait

President, October 10th, 2024

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